STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
PARSONS & WHITTEMORE INCORPORATED	:	DETERMINATION
for Redetermination of a Deficiency or for Refund of Corporation Franchise Tax under Article 9-A of the Tax Law for the Years 1978, 1979, 1980 and 1981.	:	

Petitioner, Parsons & Whittemore, Inc., 666 Third Avenue, New York, New York 10017, filed a petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the years 1978, 1979, 1980 and 1981 (File No. 802196).

On November 15, 1989 and November 10, 1989, respectively, petitioner, by Arthur R. Rosen, Esq., and the Division of Taxation, by William F. Collins, Esq. (Anne W. Murphy, Esq. of counsel) consented to have the controversy determined on submission of documents without hearing, with all documents and briefs to be submitted by June 24, 1990.

After due consideration of the record, Jean Corigliano, Administrative Law Judge, renders the following determination.

ISSUE

Whether petitioner may be required to recapture investment tax credits claimed on otherwise qualifying property on the ground that the subject property ceased to be in qualified use prior to the end of the taxable year in which the credit was taken.

FINDINGS OF FACT

On March 12, 1985 the Division of Taxation ("Division") issued to petitioner, Parsons & Whittemore, Inc., four notices of deficiency, asserting deficiencies of corporation franchise tax as follows:

Year	Deficiency

1978	$ 28,557.00
1979	187,625.00
1980	144,123.00
1981	173,267.00

Parsons & Whittemore is a New York corporation engaged in the business of providing engineering services. During the period in issue, Hempstead Resources Recovery Corporation ("HRRC") was the wholly owned subsidiary of Parsons & Whittemore. These corporations filed combined corporation franchise tax reports, along with other affiliated corporations, for the periods in issue. On reports filed for the years 1979, 1980 and 1981, investment tax credits were claimed for property located in New York and used by HRRC.

HRRC operated a solid waste disposal and recycling plant which essentially recycled garbage into electricity. The facility was constructed under the terms of an agreement with the Town of Hempstead, entered into in December 1974. Construction was completed in August 1978. The facility began operating in April 1979 but was closed in March 1980. The closing came about as a result of two events. First, a contractual dispute arose between HRRC and the Town of Hempstead, causing HRRC to refuse to accept solid waste until the dispute was resolved. At about the same time, the Environmental Protection Agency ("EPA") reported that tests conducted in 1979 indicated the presence of trace quantities of dioxin in smokestack emissions from the facility. In May 1980, then presiding Supervisor Alphonse D'Amato advised HRRC that he would not permit the operation of the plant until the EPA assured the Town that the facility operation would not pose a health threat, and, in July 1980, HRRC agreed with the Town to keep the facility closed until specific national guidelines regarding dioxin emissions were promulgated by the EPA.

At the time of the shutdown in March 1980, HRRC was in the process of installing approximately $10,000,000.00 worth of capital design improvements. These projects were 95% complete in July when the Town and HRRC made the decision to remain closed until the EPA guidelines were promulgated. The facility was placed in a "caretaking" mode until start-up became feasible. Parsons & Whittemore continued work on dioxin research, analysis of operating problems and possible technical solutions to those problems; it also conducted trials

on further improvements to the facility.

In the summer of 1982, Parsons & Whittemore began active negotiations with the Town of Hempstead to restart the facility. By this time, EPA issued a memorandum regarding dioxin emissions which apparently contained nothing which would preclude the HRRC facility from reopening. In the fall of 1982, Parsons & Whittemore employees, primarily engineers and operators, were transferred from a facility in Dade County, Florida to the HRRC facility in the Town of Hempstead to begin "demothballing" the plant.[1]

Petitioner and the Division entered into a stipulation of facts which is adopted here as Findings of Fact "5" through "9".

In accordance with a prehearing conference conducted by the former Tax Appeals Bureau, the Division of Taxation asserts a deficiency of $28,557.00 plus interest for 1978, asserts no deficiency for 1979, admits a refund of $54,874.00 for 1980, and asserts a deficiency of $175,767.00 for 1981.

The deficiency for 1981 results from the Division requiring certain credits allowed in prior years pursuant to Tax Law § 210.12(a) ("investment tax credits") to be added to the tax otherwise due ("recaptured") in 1981 pursuant to Tax Law § 210.12(g). The Division asserts that the subject property ceased to be in qualified use because it was no longer being used in the production of goods by manufacturing.

At the prehearing conference the investment tax credits sought to be recaptured by the 1979 and 1980 deficiencies were properly allowed for those years when the subject property was initially placed in service. The Division of Taxation agrees to the adjustments. On field audit, the Division determined that identified items of plant, machinery and equipment on which investment tax credits were claimed, met the requirements of Tax Law § 210.12(b).

---

[1]In its brief, the Division states that the plant never became operational. In its reply brief, petitioner asserts that the plant was sold in 1986 and began operating after being substantially retrofitted by the new owner to satisfy EPA guidelines.

During 1981, due to circumstances beyond petitioner's control, the facility in which the subject property was located was not in operation, but throughout 1981 and thereafter, petitioner planned to recommence operations as soon as possible.

No recapture of the Federal investment tax credit (pursuant to Internal Revenue Code § 47[a][1] and [5]) would be required for 1981 because the subject property was not disposed of or abandoned during 1981.

The HRRC property upon which investment tax credits were claimed included: a conveying system, wet processing equipment, an iron recovery system, glass and aluminum recovery equipment, boilers, turbo-generators, a pit and unloading building, a process and recovery building, a fuel storage building and a generation building used to house the turbo-generators.

Petitioner has raised no issues with regard to the 1978 tax year. The only issue raised in this proceeding is whether petitioner may be required to recapture the investment tax credits claimed for periods subsequent to March 1980, resulting in a tax deficiency in 1981 of $175,767.00.

CONCLUSIONS OF LAW

A. Tax Law § 210.12(b) provides for a credit against tax, the investment tax credit, with respect to certain tangible personal property and other tangible property, including buildings and structural components of buildings. To qualify for the credit, the property must:

(1) be depreciable under section 167 of the Internal Revenue Code or be recovery property with respect to which a deduction is allowable under section 168 of the Internal Revenue Code;

(2) have a useful life of four or more years;

(3) be acquired by the taxpayer by purchase as defined in section 179 of the Internal Revenue Code; and,

(4) as relevant here, be used principally by the taxpayer in producing goods by manufacturing, processing, assembling or refining (Tax Law § 210.12[b]; 20 NYCRR 5-2.2).

If property on which an investment tax credit has been allowed "is disposed of or ceases to be in qualified use" prior to the end of its useful life, the difference between the original credit and the credit allowed for actual use must be added back to the tax otherwise due in the year of disposition or disqualification (i.e., "recaptured") (Tax Law § 210.12[g][1]; 20 NYCRR 5-2.8[a]).

Property is no longer qualified for the investment tax credit if any of the following events occurs:

(1) The taxpayer disposes of the property. Dispositions include: sales, liquidations (other than a transfer as part of a transaction to which IRC § 381[a] applies), legal dissolution of the taxpayer, trade-ins or exchanges, gifts, transfers on foreclosures of a security interest, retirements from service, condemnations, casualty losses and transfers to corporations not subject to the New York business corporations tax (20 NYCRR 5-2.8[c], [e]).

(2) The property no longer has a New York situs (20 NYCRR 5-2.8[d][1]).

(3) The property is leased to others (20 NYCRR 5-2.8[d][2]).

(4) The property is "no longer used in the production of goods" (20 NYCRR 5-2.8[d][1]).

B. The parties agree that the HRRC property was "qualified property" (20 NYCRR 5-2.2[a]) from the time it was placed in service in 1979 until the entire facility was closed in March 1980. It is the Division's position that the HRRC property ceased to qualify for the credit after the facility closed in 1980. This position is based primarily upon a reading of the relevant statutes and regulations. The Division argues that an idled plant and machinery are "no longer principally used by the taxpayer in the production of goods" (Tax Law § 210.12[b]; 20 NYCRR 5-2.8[d][1]) and, therefore, have ceased to be in "qualified use" (Tax Law § 210.12[g][1]). Petitioner contends that the HRRC property continued to be used in the conduct of HRRC's trade or business, and, inasmuch as that business was the production of goods by manufacturing, the property continued to be in "qualified use".

C. Neither of the parties has cited to any New York authority to support its interpretation of section 210.12(g)(1). Petitioner relies primarily on Federal authority to support its position.

An interpretation of the State tax law is not necessarily mandated by Federal interpretations of similar provisions; however, in the absence of clear legislative intent or compelling reasons to the contrary, it is appropriate to look to Federal authority for guidance in interpreting similar or analagous State tax provisions (see, Matter of John Grace & Company, Tax Appeals Tribunal, May 10, 1990; Matter of Accessories By Pearl, Tax Appeals Tribunal, February 24, 1989). The Division concedes that, where appropriate, conformity with Federal corporation income tax provisions is favored; however, it argues that application of Federal authority would be inappropriate in this case, essentially because of what it perceives to be dissimilarities in the Federal and State investment tax credit provisions. This determination begins then with a brief, and necessarily simplified, comparison of the relevant Federal and State investment tax credit provisions.

The Federal investment tax credit provisions were enacted into law by the Revenue Act of 1962 (Pub. L. No. 87-834, 76 Stat. 962 [1962]). The purpose of enacting the investment tax credit was to stimulate domestic investment by reducing the net cost of acquiring depreciable assets and increasing the flow of cash available for investment (1962 US Code Cong & Admin News 3304, 3313-3314). Property which qualifies for the Federal credit is termed "section 38 property" and, in general, is depreciable tangible personal property (IRC § 48[a][1]; Treas Reg § 1.48-1[a]). Generally, depreciable property is property used in the taxpayer's trade or business or held for production of income (IRC § 167[a]). In addition to tangible personal property, other tangible property, excluding land, buildings, or other inherently permanent structures, is section 38 property, provided such property is used in one of several enumerated activities, including: as an integral part of manufacturing or production (IRC § 48[a][1][B]).

The State investment tax credit was adopted in 1969 (L 1969, ch 1072). The purpose of the legislation was to "[e]ncourage the modernization of antiquated production facilities and make New York a more attractive location for manufacturers by giving a tax credit for new investments in production facilities" (Legislative Memorandum, Governor's Bill Jacket, L 1969, ch 1072). The investment tax credit provisions rely on the Internal Revenue Code in several

instances: the amount of the credit is calculated as a percentage applied to "the cost or other basis for federal income tax purposes of tangible personal property and other tangible property" (Tax Law § 210.12[a]), and section 210.12(b) refers directly to several provisions of the Code in listing the criteria which must be met for eligibility. There are, however, significant differences between the Federal and State law with respect to property eligible for the credit. Most significantly for the issues raised here, New York extends the credit only to tangible personal property and other tangible property, including buildings and their structural components, "principally used by the taxpayer in the production of goods" (Tax Law § 210.12[b]). Thus, the New York credit is both narrower (in limiting the credit to production facilities) and broader (in extending the credit to buildings and their structural components) than the Federal credit. The fact that the Federal and State provisions are not identical does not warrant a conclusion that Federal authority is irrelevant to the issue raised here (see, Matter of John Grace & Company, supra). In fact, there is some precedent for relying on the Federal law for guidance in interpreting section 210.12(b) of the Tax Law (see, Matter of Noris J. Stone & Sons, State Tax Commission, February 29, 1984 [TSB-H-87(29)C]). Moreover, the language of the Federal and State recapture provisions are substantially the same. Tax Law § 210.12(g)(1) provides for a recapture of credits for property which "is disposed of or ceases to be in qualified use" (emphasis added). IRC § 47(a)(1) provides for a recapture of credits for property which "is disposed of, or otherwise ceases to be section 38 property" (emphasis added). The Division argues that Federal investment tax credits are recaptured in only one instance, i.e., when there is an early disposition of otherwise qualifying property, while State credits are recaptured under two different circumstances: either (1) early disposition or (2) when property ceases to be in qualified use. That interpretation of the Federal statute is contradicted by the Treasury Regulations. Treas Reg § 1.47-2(a)(2) provides as follows:

> "(2) 'Cessation'. (i) A determination of whether section 38 property ceases to be section 38 property with respect to the taxpayer must be made for each taxable year subsequent to the credit year. Thus, in each such taxable year the taxpayer must determine, as if such property were placed in service in such taxable year, whether such property would qualify as section 38 property (within the meaning of § 1.48-1) in the hands of the taxpayer for such taxable year.

> (ii) Section 38 property does not cease to be section 38 property with respect to the taxpayer in any taxable year subsequent to the credit year merely because under the taxpayer's depreciation practice no deduction for depreciation with respect to such property is allowable to the taxpayer for the taxable year, provided that the property continues to be used in the taxpayer's trade or business (or in the production of income) and otherwise qualifies as section 38 property with respect to the taxpayer."

Thus, both Federal and State law require the recapture of tax credits when property ceases to be used for a statutorily qualified purpose. Because of the similarities between the Federal and State investment tax credit provisions generally, and the recapture provisions in particular, it is appropriate to look to Federal authority for guidance here.[2]

D. The search by petitioner and this administrative law judge disclosed only one case which considered the circumstances under which property "ceases to be section 38 property" under IRC § 47(a)(1). In that case, the court found that "section 47 is designed to preclude a taxpayer from receiving the tax benefit of the investment credit and then failing to use the section 38 property in the taxpayer's trade or business for the entire useful life upon which the credit was calculated" (Panhandle Eastern Pipeline Co. v. United States, 654 F2d 35, 81-2 US Tax Cas ¶ 9496). Unfortunately, this case provides little guidance with regard to when section 38 property ceases to be used in a taxpayer's trade or business, offering as an example of such circumstances only a situation in which property is put to personal use.

Although there is no case law directly on point, there is a body of Federal law concerning an analagous issue: when should property be deemed to have been "placed in service" for purpose of qualifying for the Federal

investment tax credit.[3] The applicable regulation with respect to this issue is found at Treas Reg

---

[2]The Division has itself relied on Federal law in interpreting section 210.12(g) (see Advisory Opinion, Commissioner of Taxation and Finance, August 11, 1988 [TSB-A-87(16)C], relying on Treas Reg § 1.47-3 to interpret the word "disposition" as used in section 210.12[g][1] of the Tax Law and 20 NYCRR 5-2.8).

[3]Treas Reg § 1.47-2(a)(2), quoted above, requires that a separate determination be made for each taxable year subsequent to the credit year with respect to whether property has ceased to be section 38 property. The taxpayer is required to "determine, as if such property were placed in

§ 1.46-3(d) which reads as follows:

> "(1) For purposes of the credit allowed by section 38, property shall be considered placed in service in the earlier of the following taxable years:
>
> (i) The taxable year in which, under the taxpayer's depreciation practice, the period for depreciation with respect to such property begins; or
>
> (ii) The taxable year in which the property is placed in a condition or state of readiness and availability for a specifically assigned function, whether in a trade or business, in the production of income, in a tax-exempt activity, or in a personal activity."

Treas Reg § 1.167(a)-11(e)(1)(ii), explaining the depreciation deduction, contains a similar provision using almost identical language. The weight of Federal authority holds that a facility should be deemed placed in service and in a condition or state of readiness and availability for a specifically assigned function when the facility is determined to be operational, whether or not it is actually used during the taxable year. In Sears Oil Co. v. Commissioner (359 F2d 191, 66-1 US Tax Cas ¶ 9384), a barge was delivered to the taxpayer in New York in the fall of 1957; because the barge was frozen in a canal, it was not put into use until spring of 1958. The court held that the barge was eligible for depreciation (and accordingly used in a trade or business) by December 1, 1957, since it was ready for use and subject to deterioration due to aging and exposure to the

elements. Based on the reasoning in Sears, the court in SMC Corp. v. United States (675 F2d 113, 82-1 US Tax Cas ¶ 9309, affg 80-2 US Tax Cas ¶ 9642) held that equipment was placed in service and therefore eligible for the investment tax credit even though it was not actually used during the year in question because of a lack of permanent electrical connections. In W. R. Waddell v. Commissioner (86 TC 848, affd 841 F2d 264), an investment credit was allowed for the year in which the taxpayer technically acquired, but never actually took possession of, certain medical diagnostic terminals. The court stated: "for purpose of the investment credit, it

---

service in such taxable year, whether such property would qualify as section 38 property (within the meaning of § 1.48-1)" (Treas Reg § 1.47-2[a][2][i] [emphasis added]).

is not necessary that the property actually be used during the credit year" (id. at 897).

With respect to the issues raised here, the most significant difference between the State and Federal investment tax credit provisions is the criteria for eligibility. As relevant to this discussion, the Federal credit applies to all tangible personal property used in the the taxpayer's trade or business (or for the production of income), while the State credit applies only to property used in the production of goods. However, the Federal credit also applies to other tangible property, provided that that property is used "as an integral part of manufacturing". Thus, there is a similarity between the Federal and State provisions with regard to property held to be "other tangible property" under section 48(a)(1) of the Internal Revenue Code. Since the property in Fort Howard Paper Co. v. Commissioner (36 TCM 1711) was found to be "other tangible property", the holding there is especially relevant here. The taxpayer in that case claimed investment tax credits for the costs of constructing a power plant addition which included a turbine room intended to house two turbines. Only one of the turbines was installed in 1970. The second turbine was not installed until 1976. Initially, the Commissioner contended that the turbine room was a building and as such not eligible for the investment tax credit. The court disagreed, holding that the turbine room was "other tangible property" and "used as an integral part of manufacturing" (IRC § 48[a][1][B][i]). It then went on to consider whether the portion of the turbine room reserved for the second turbine was "placed in service" during 1970, as required by IRC § 46(c)(1)(A). Because the turbine room was ready and available for the second turbine, it was deemed to have been placed in service in 1970 and eligible for the investment tax credit in that year. (Id. at 1720-1723.)

Clearly, the rationale of the Federal cases supports petitioner's argument that property is "used" in the production of goods if it has been placed in service and is ready and available for use, even if is not in actual usage during the period for which the credit is claimed. The problem with the Division's interpretation of the statute is that it would trigger the recapture provision whenever a facility was temporarily closed. If, for example, a labor strike or economic recession caused a manufacturing plant to close for a period of time, the Division's

interpretation of section 210(g)(1) would deny the taxpayer an investment tax credit for that period, even though the property continued to be depreciable during that time. Furthermore, there is no evidence that the Legislature intended a recapture of credit during periods of temporary non-usage.

The situation here is somewhat different from those discussed in the cited Federal cases in that HRRC never reopened the facility, but eventually sold it to another operator. Nonetheless, the evidence shows that petitioner intended to reopen the facility in 1980 and 1981. At the time of the shutdown, HRRC was in the process of installing capital design improvements, negotiations with the Town of Hempstead to reopen continued through 1982 and petitioner was conducting research in dioxin emissions and operating problems and conducted trials on further improvements to the facility. Since the property on which the credit was claimed was ready and available for an assigned function which was the production of goods by manufacture or processing, it is concluded that the property was in qualified use in 1980 and 1981; therefore, petitioner was entitled to the investment tax credit in both years.

E. The parties have stipulated that the tax deficiencies asserted by the Division are as follows: $28,557.00 plus interest for 1978; no deficiency for 1979; a refund of $54,874.00 for 1980; and a deficiency of $175,767.00 for 1981. The deficiency asserted for 1981 will be recomputed by the Division in accordance with Conclusion of Law "D".

F. The petition of Parsons & Whittemore is granted to the extent indicated in Conclusions of Law "D" and "E"; the notices of deficiency issued on March 12, 1985 shall be modified accordingly; and in all other respects, the petition is denied.

DATED: Troy, New York

_____

ADMINISTRATIVE LAW JUDGE